STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Date Introduced	**2/23/01**	Bill No:	**SB 882**
Tax:	**Property**	Author:	**O'Connell**
Board Position:	**Support**	Related Bills:	**SB 2172 (2000)**

BILL SUMMARY

This bill would exempt a leasehold interest in a public park held by a charitable foundation that will acquire ownership of the park at the end of the lease term.

ANALYSIS

Current Law

Under existing property tax law, real property is reassessed to its current fair market value whenever there is a "change in ownership." (*Article XIIIA, Sec. 2; Revenue and Taxation Code Sections 60 - 69.7)*

When property is subject to a lease, in tracking whether a change in ownership occurs, the "owner" of the property is considered to be either the lessee or the lessor depending upon the term of the lease and the point in time of the lease. This is done to identify a "primary owner" of the property, so that only a transfer of that person's interest in the real property will be a change in ownership. Generally when the lease term is for 35 or more years, the lessee's interest is tracked for change in ownership purposes rather than the actual owner of the property. The interest in property for a 35 year term is considered to be equivalent in value to fee ownership. Generally, with respect to property that is leased, as it relates to this bill, a "change in ownership" occurs

- upon the creation of a leasehold interest for a term of 35 years or more, or
- upon the transfer of a leasehold interest having a remaining term of 35 years or more.

Under existing law, certain property owned and operated by nonprofit organizations for charitable purposes may be exempt from property tax under the "welfare exemption." (Revenue and Taxation Code Section 214)

To qualify for the welfare exemption, the property must be owned and operated by a qualifying organization that meets all the requirements for exemption. Under existing law, one condition is that the organization *owns* the property. Property that is leased or rented by an otherwise qualified applicant is ineligible for welfare exemption. Thus, while existing law provides that a 35-year lease is equivalent in value to fee ownership for change in ownership reassessment purposes, it does not similarly provide that it is "ownership" for purposes of the welfare exemption.

Proposed Law

This bill would add Section 236.5 to the Revenue and Taxation Code to provide that any otherwise taxable interest in real property, leased for an original term of 35 years or more and used exclusively by the lessee for the operation of a public park, is, during the term of the lease, within the exemption provided for in subdivision (b) of Section 4 and Section 5 of Article XIII of the California Constitution, if all of the following conditions are met:

1. The lessee is a charitable foundation that has received a determination that it is a charitable organization as described in Section 501(c)(3) of the Internal Revenue Code.
2. The operation of the public park by the lessee is within the tax exempt purposes of the lessee.
3. The lessee acquired the leasehold in the property by means of a charitable donation.
4. Under the terms of the lease, the lessee will acquire the entire ownership interest in the property at the end of the lease term.

Background

Wynmark Company and its partners constructed a public park, Lester A. & Viola S. Girsh Park in Goleta, California http://www.girshpark.org and donated it to a nonprofit foundation, the Camino Real Park Foundation, which was established to operate the park. The company currently has a long term lease in the land and will acquire fee ownership of the land in 20 years, at which point it will donate the full fee simple ownership of the park and land to the nonprofit foundation. Currently, the foundation has a 70-year lease in the park but will acquire full ownership of the park before the end of the lease in another 20 years. The transfer of the leasehold interest from Wynmark Park to the foundation was a change in ownership of the property requiring reassessment to current fair market value since the term of the lease exceeded 35 years.

COMMENTS

1. **Sponsor and Purpose.** This bill is sponsored by the author to provide an exemption for a public park that is leased to a non-profit organization. Under current law, the park will not be exempt from property tax under the welfare exemption until the non-profit organization acquires fee ownership of the property in 20 years.
2. **Under the circumstances outlined in this bill, property tax law considers a nonprofit organization to be the "owner" of the property for change in ownership purposes, but not for welfare exemption.** Girsh Park in Goleta is a community park, currently leased to a nonprofit foundation formed to operate the park, as explained under Background. The property was recently reassessed to current fair market value as a "change in ownership" because the lease term exceeded 35 years. For change in ownership purposes, the foundation was

considered to be the "primary owner" of the property. But the nonprofit foundation cannot receive the welfare exemption on the property, because under those provisions of law, it is not the "owner" of the property. The foundation will acquire "fee" ownership of the property in about 20 years. Once fee ownership is acquired, the property would be eligible for exemption from property taxes under existing law.

3. **Generally, property that is leased cannot qualify for the welfare exemption.** Section 3 and Section 4 of Article XIII of the California Constitution differ with respect to the ownership requirement for certain property tax exemptions therein provided. Section 3 exempts property *used* (i.e. ownership is not required) for (1) libraries and museums that are free and open to the public, (2) public schools, colleges, and universities, and (3) religious worship. Section 4 exempts property *used* exclusively for religious, hospital and charitable purposes *and owned or held in trust* by nonprofit entities organized and operated for those purposes. The terms "own," "held in trust," and "used" are not defined in the constitution. Thus, it could be argued that the Legislature could define "ownership" for the welfare exemption to include this type of long term lease arrangement as has been done for change in ownership purposes.

4. **Existing law provides a similar exception for long-term leases of property used for low-income housing.** The provisions proposed by this bill are similar to those of Revenue and Taxation Code Section 236, which exempts property used for rental housing for low-income persons which is leased for a term of 35 years or more (or any transfer of such property leased with a remaining term of 35 years or more) when the lessor is not otherwise qualified for the welfare exemption pursuant to Section 214. Section 236 recognizes that the lessor is not qualified for the welfare exemption but has no requirement that the qualifying lessee acquire the fee interest at the end of the lease term.

5. **Most public parks are exempt from property tax because state or local governments own them.** It may become more common for private charitable foundations to operate public parks if government resources cannot fulfill the demand. In the future, where developers are required to set aside open space and public park land as a condition of development approval, local governments may not have the funds needed to maintain them, which could lead to more situations where parks are operated, but not owned, by charitable foundations.

6. **"Public Park" is not defined.** Should it be limited to parks "uniquely of a government character," as provided in Section 231(b)(4), i.e. a traditional community park, accessible and "free" to the public, to the same extent government owned parks are accessible and free.

7. **Technical consideration**. One condition for the proposed exemption is that "under the terms of the lease, the lessee will acquire the entire ownership interest in the property at the end of the lease term." However, it appears that the foundation will technically acquire ownership before the end of the lease. If this is the case, perhaps some amendment is needed to include this situation as well, "on or before the end of the lease term."

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

8. **Related Legislation.** This bill is identical to a provision amended into SB 2172 (Chesbro) near the end of the 2000 legislative session. Those amendments were made on August 22 and deleted out of that bill on September 12.

Cost Estimate

With respect to property taxes, the Board would incur some minor absorbable costs in informing local county assessors, the public, and staff of the law changes.

Revenue Estimate

Background, Methodology, and Assumptions

Existing property tax law establishes, pursuant to the authorization of the California Constitution, a welfare exemption under which property is exempt from taxation if, among other things, that property is used exclusively for religious, hospital, scientific, or charitable purposes and is owned and operated by an entity, as provided, that is itself organized and operated for those purposes. In addition, under current law, the real property must be held in fee ownership by the entity to qualify for the exemption.

Under this proposal, the welfare exemption would extend to any otherwise taxable interest in real property that is leased for a term of 35 years or more by a charitable foundation, exempt from federal income taxation, if the real property is used exclusively by the lessee for operation as a public park, the lessee acquired the leasehold in the property by means of a charitable contribution, and the lessee foundation is, under the terms of the lease, to obtain fee ownership of the property at the end of the lease term.

Currently, there is only one charitable foundation that appears to qualify under this proposal: Camino Real Park Foundation. This organization is responsible for the operation of Lester A. and Viola S. Girsh Park in Goleta, California. A 70-year leasehold interest was donated to the Foundation for the park. Upon the donor's formal acquisition of the leased property within the next twenty years, actual fee simple ownership will be transferred to the Foundation for $1.00. The property will then qualify for the welfare exemption because the Foundation will hold fee simple title.

According to the Santa Barbara County Assessor's Office, the assessed value of the park is $4.1 million. Therefore, the initial annual revenue impact from exempting the property from the basic one percent tax rate is $41,000 ($4.1 million x .01).

Revenue Summary

The estimated annual revenue impact at the basic one percent property tax rate from exempting the real property that would qualify under this proposal is a decrease of $41,000. It is likely that this loss will grow slightly over time due to the Proposition 13 inflation factor until the fee simple ownership of the subject property is transferred to the Foundation.

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Qualifying Remarks

The above estimate applies only to Girsh Park, as mentioned in the background section above. While it is possible that the adoption of this bill could encourage other charitable organizations to engage in similar undertakings, because of the stated limitations in the language of this bill, that likelihood is considered remote.

Analysis prepared by:	Rose Marie Kinnee	445-6777	3/12/01
Revenue estimate by:	Aileen Tanaka Lee	445-0840	
Contact:	Margaret S. Shedd	322-2376	

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